



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS**

Draft

Date Amended	08/21/01	Bill No:	AB 984
Tax:	Sales and Use	Author:	Papan
Board Position:	Support	Related Bills:	

BILL SUMMARY

This bill would provide a sales and use tax exemption until January 1, 2004, for the sale and leaseback of public passenger transportation vehicles when sold or leased by a transit authority, special district, or governmental entity.

ANALYSIS

Current Law

Under the existing sales and use tax law, sales or use tax applies to the sale or use of all tangible personal property, unless specifically exempted. Generally, a sale includes any lease of tangible personal property for a consideration. However, leases of mobile transportation equipment are specifically excluded from the definition of a "sale." Mobile transportation equipment (MTE) includes equipment such as railroad cars, buses, trucks, tractors, aircraft and ships. The lessor of MTE is regarded as the consumer of the property and tax applies to the retail sale to the lessor, unless the lessor makes a timely election to report tax on the fair rental value.

Proposed Law

This bill would add Section 6368.8 to the Sales and Use Tax Law to provide an exemption from the sales and use tax for the sale in this state of, or the storage, use, or other consumption in this state of qualified equipment sold or leased by a qualified person and leased or subleased back to that qualified person. To qualify for the proposed exemption, the qualified equipment must be sold or leased by a qualified person, the qualified person must have paid sales tax reimbursement or use tax with respect to the acquisition of the qualified equipment, and the qualified equipment must be sold or leased back to the qualified person.

This bill would define "qualified equipment" to mean a vehicle or vessel and any related equipment used in the provision of public passenger transportation services, including, but not limited to, bus and van fleets, ferry boats, rail passenger cars, locomotives, other rail vehicles, train control equipment, communication systems, global positioning systems, and other systems and accessories related to the operation of a vehicle or vessel used in the provision of public transportation services.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

This bill would define “qualified person” as an entity that qualifies as a claimant, as defined in Section 99203 of the Public Utilities Code, eligible to receive allocations under the Transportation Development Act (commencing with Section 99200 of the Public Utilities Code).

This bill would also provide that the proposed exemption apply to subsequent purchases of qualified equipment by a qualified person at the end of the term of a lease or sublease of qualified equipment.

This bill would become operative on the first day of the first calendar *month* commencing more than 15 days after the effective date. The provisions of this bill would remain in effect only until January 1, 2004, and as of that date would be repealed.

This bill would also require the Legislative Analyst, in consultation with the State Board of Equalization and the Franchise Tax Board, to conduct a study on the impact of the proposed exemption and submit a report to the Legislature by January 1, 2003. The report would contain the number of persons utilizing the proposed exemption, the fiscal impact of the exemption including the total exemption amount and any depreciation claimed for qualified equipment, the impact of federal law on the utilization of the exemption, the impact of the exemption on California’s public transit sector, and a recommendation as to whether the exemption should be extended beyond the January 1, 2004 expiration date, and if it is recommended that the exemption should be extended, recommendations on modifications to the exemption provisions proposed in this bill.

In General

Since 1990, a number of California transit agencies have sought to generate additional revenues by entering into transactions which transfer the depreciation attributes of an asset, such as passenger rail cars or buses, to a private taxable entity. Such arrangements are described as a “sale and leaseback.” The transaction allows the private firm to take federal income tax deductions, while permitting the equipment to be used by the transit agency for its intended public purpose of providing transit services. In exchange for participating in the transaction, the transit agency receives an up-front payment from the private firm. The up-front payment from the private firm is enough to cover the lease payments over the term of the lease, plus a premium of 6-8 percent of the equipment cost. This 6-8 percent premium is revenue the transit agency can use to meet future transit capital or operating needs.

The transit agency pays sales or use tax on the initial purchase of the equipment. However, if a transit agency were to enter into a sale and leaseback under current law, the sale by the transit agency to the purchaser/lessor would also be subject to sales or use tax. This additional sales or use tax expense would offset the 6-8 percent premium that the transit agency would have received. Due to the imposition of the sales and use tax, there is no financial benefit for either party to enter into such a transaction.

Background

Assembly Bill 3382 (Ch. 558, Stats. 1990) provided that a “sale” and “purchase” does not include any transfer of title to, nor any lease of, tangible personal property pursuant *This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board’s formal position.*

to an acquisition sales and leaseback. To qualify as an acquisition sale and leaseback, the person must have paid sales tax reimbursement or use tax on the purchase price of the property and the acquisition sale and leaseback must be consummated within 90 days of the person's first functional use of the property. In practice, many of the assets held by a transit agency have been functionally used for more than 90 days, so the acquisition sale and leaseback provisions would not apply.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the California Transit Association and is intended to provide a means for transit agencies to enter into sale and leaseback transactions without the penalty of paying the sales or use tax twice.
2. **Summary of August 21 amendments.** Amendments in this version of the bill changed the operative date to the first day of the calendar month commencing more than 15 days after the effective dates of this act, the addition of a January 1, 2004 sunset date, and the requirement that the Legislative Analyst, in consultation with the Board of Equalization and the Franchise Tax Board, submit a report to the Legislature by January 1, 2003 on the impact and utilization of the proposed exemption.
3. **Income tax benefit is not available to transit agencies.** Since transit agencies do not pay income taxes, they have no way to depreciate their assets for income tax purposes. This bill would allow the transit agency to transfer the income tax benefit to another entity in exchange for a share of the benefit.
4. **Definition of a qualified person.** The proposed exemption would only be available to a qualified person. This bill defines a qualified person to mean an entity that qualifies as a claimant, as defined in Section 99203 of the Public Utilities Code, eligible to receive allocations under Transportation Development Act (commencing with Section 99200 of the Public Utilities Code). Section 99203 of the Public Utilities Code defines a "claimant," or any derivative term, such as "applicant," to mean an operator, city, county, or consolidated transportation service agency.
5. **Report to the Legislature would be required.** The provisions of this bill would require the Legislative Analyst, in consultation with the State Board of Equalization and the Franchise Tax Board, to conduct a study on the impact of the proposed exemption and submit a report to the Legislature by January 1, 2003. The report would contain the number of persons utilizing the proposed exemption. The Board would have to maintain records of these exemptions for the report.
6. **This bill would not be problematic to administer.** The provisions of this bill would apply to a limited number of transactions and would not be difficult for the Board to administer. However, the proposed exemption would become operative on the first day of the first calendar month commencing more than 15 days after the effective date of the bill. This could leave the Board with as little as 15 days to prepare to administer the proposed exemption prior to the exemption actually becoming operative.

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COST ESTIMATE

Some costs would be incurred in revising returns, regulations and publications. Due to the potential short period of time between effective date and the operative date, a special notice mailing may be required to notify affected parties of the proposed exemption. While it is unknown at this time how many notices must be sent, these costs are expected to be less than \$10,000.

REVENUE ESTIMATE

Background, Methodology, and Assumptions

This proposal would exempt the sale/leaseback or lease/leaseback transactions that transit agencies might enter into. Under these types of arrangements, the transit district would either sell or lease vehicles, for which the sales or use tax has already been paid on the original acquisition, to a private entity. The private entity would then lease the vehicles back to the transit authority. The transaction in effect transfers the tax depreciation attributes of the vehicles to the private entity. The transit authority uses the vehicles for public transit services and receives an up-front payment from the private entity.

These types of transactions are currently exempt, if the sale/leaseback transaction occurs within 90 days of the first functional use of the vehicles by the transit agency. This proposal would extend the exemption for these transactions to all public transportation vehicles rather than to only newly purchased vehicles.

The California Transit Association states that no such sale/leaseback arrangements for older vehicles currently exist and unless this proposal is adopted, it would not be cost effective for transit agencies to enter into such sale/leaseback arrangements.

Revenue Summary

There would not be any current sales and use tax revenue impact from exempting from the sales and use tax sale/leaseback or lease/leaseback agreements concerning public passenger transportation vehicles as no such agreements exist now or would be entered into without this exemption.

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